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PEOPLE'S BANKS

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SOME PUBLICATIONS ON CO-OPERATIVE CREDIT ISSUED BY RUSSELL SAGE FOUNDATION

No. 5. **Co-operative Credit.** A Selected Bibliography. Bulletin of Russell Sage Foundation Library, June, 1914. (5 cents.)

RL 15. **A Credit Union Primer.** By Arthur H. Ham and Leonard G. Robinson.
Contains a brief history of co-operative credit, a definition of its field in the United States, an outline of the elementary principles of credit unionism, together with model by-laws, necessary books and forms, instructions for organizing, and the New York credit union law.
Division of Remedial Loans. 79 p. 1914. (25 cents.)

RL 16. **The Co-operative People's Bank.** By Alphonse Desjardins.
The evolution of the co-operative bank, the Canadian system, its growth and accomplishments.
Division of Remedial Loans. 42 p. 1914. (15 cents.)

RL 19. **Credit Unions and their Relation to Savings and Loan Associations.** By Arthur H. Ham.
An address delivered before the State League of Savings and Loan Associations, Port Jervis, N. Y., June 10, 1915.
Division of Remedial Loans. 12 p. 1915. (Single copies free.)

RL 22. **Determining Credit.** A Suggestive Method for Credit Committees of Credit Unions. Devised by R. S. Hale.
Division of Remedial Loans. 8 p. 1916. (Single copies free.)

RL 23. **The Object of the Credit Union.** A Reply to Myron T. Herrick. By Arthur H. Ham.
Division of Remedial Loans. 12 p. 1916. (Single copies free.)

RL 24. **People's Banks.** By Arthur H. Ham.
Division of Remedial Loans. 16 p. 1916. (Single copies free.)

RL 27. **Credit Unions (Co-operative People's Bank), Their Development and Purpose.** In Yiddish. By Morris Caesar.
Division of Remedial Loans. 52 p. 1916. (25 cents.)

PEOPLE'S BANKS

Among the obstacles that lie in the path of the modern program for the improvement of social and living conditions in all the respects of health, efficiency, material welfare, recreation and intellectual advancement none looms larger than these: (a) the lack of thrift in American families, (b) the many forms of waste and exploitation surrounding the purchase of necessities, and (c) the lack of reasonable credit by means of which emergency needs may be met. In spite of its extravagant and wasteful methods of living the family usually manages to provide itself with the necessities of life and it is the call for extraordinary financial outlay, unforeseen and unprovided for, that marks the beginning of the fall of most families which claim the attention of the relief societies.

There is a time-honored delusion that thrift is represented by savings bank deposits and commentators of American unthrift are fond of comparing the $48 per capita average of savings bank deposits in the United States with the larger average of certain European countries. A writer in a popular magazine recently, to prove us a prodigal people, went so far as to move the decimal point one place to the left and credit us with a per capita average deposit of only $4.84. Such comparisons invariably fail to include the two billions and over of individual deposits held by trust companies and commercial banks and $1,300,000,000 deposited in the 6,600 building and loan associations throughout the country. They fail to take into account numerous other factors, such as the great sums invested in small securities. This is well illustrated by the steady decline in recent years of net deposits in the New York savings banks which is attributed by well-informed bankers not to decreased savings but to the growth of "investment intelligence" which has led many people who formerly deposited their savings to buy small partici-

pating mortgage certificates and good stocks and bonds issued in small denominations.

Though the average of savings deposits is not a real indictment of American thrift and foresight there is no lack of evidence of unthrift in the wasteful and uneconomic use of income by American families. Out of the weekly wage many a family can buy what it has to in the way of necessities but it cannot so apportion its expenditures as to permit buying in large quantities and so effect a saving. Cheap amusements, reading matter and such things are within its reach, but the purchase of winter clothes or household equipment often presents as great a problem as the payment of hospital expenses.

The device employed by business to meet these conditions is the instalment agency from which the family may procure clothing, furniture, etc., and pay for it in small regular instalments out of income. Unfortunately this agency in unscrupulous hands has been used not only as a means of enticing people to purchase unnecessary articles but also to reap a profit far beyond a reasonable interest on deferred payments or proper compensation for risk involved in such credit transactions—thus becoming an important contributing cause of poverty and distress.

Credit is founded on confidence, i. e., the trust that the lender has in the reliability of the borrower and his ability to meet his obligation when due. Commerce depends on credit, production cannot go on without it and there are times when the ability to obtain a loan is of the utmost advantage to a workingman. Banks are the machinery by which credit is converted into money but the workingman turns to the banks for temporary help only to find that their services are not available for him,—that confidence on which credit is based comes from a belief in the solvency and efficiency as well as the integrity of the borrower. Character, capability and capital are the tests on which banking credit depends and the needy wage earner, regardless of his unassailable honesty, sobriety, and industry, is insolvent and so cannot qualify. Some time ago the country was startled by the alleged statement of the late J. P. Morgan before a congressional committee that "Character is the basis of credit." He was not quoted quite correctly. What he said in answer to the question, "Is not commercial credit based primarily on money or prop-

erty?" was, "No, the first thing is character." He enunciated no new principle in banking. He merely neglected to say that the other co-essentials of credit are capability and capital.

The savings bank cannot loan to the wage earner because of legal restrictions limiting it to investment in approved bonds and real estate mortgages. The commercial bank will not loan to him because he cannot satisfy its requirements as to security and, besides, his loan is too small to bother with. Our vast array of savings institutions mobilizes the savings of the people, not for use by the classes that assisted in the accumulation, but by large commercial and industrial borrowers. They are "People's Banks" at the receiving teller's window but something else at the loans and discounts counter.

Overtaken by illness in his family or other emergency, facing the danger of losing an insurance policy through lapse in premium, of losing his equity in his home through arrearages in taxes or of losing his household goods through inability to meet the extortionate demands of the instalment shark, the workingman turns to the agency always advertising its readiness to come to the assistance of unfortunates—the professional money-lender, commonly referred to by those who know his characteristics as the "loan shark." From this good angel the needy man may obtain a loan on security of pledge or mortgage of his personal property, assignment of wages, or the endorsement of a friend, at an interest charge of from 100% per annum upwards, and thereby begins a chain of transactions which, except in rare instances, leads to greatly increased distress and often to theft, family desertion and suicide.

Recognizing the need for and the legitimate uses of credit in the economy of the wage earner and the parasitic character of the loan shark who fattens upon his need, there came into existence the remedial loan agency formed by public-spirited men not primarily for gain but for the purpose of demonstrating that the small loan business which has always been considered extra-hazardous is not in reality fraught with unusual risk when properly conducted and that under methods based on higher standards of business morality than the loan shark employs, the business can be successfully and profitably conducted at rates very much lower than those which have long prevailed. In

this respect the remedial loan societies, from the great Provident Loan Society of New York to the chattel mortgage associations employing but a few thousands of capital, have been conspicuously successful. They have not sought to monopolize the small loan business but their competition has been sufficient to force professional money-lenders in a great many cities to reduce their charges to a reasonable level. Their influence has assisted in securing the passage of adequate legislation in a large number of states and their example has attracted reputable capital into the business, without thought of philanthropy, but in the belief that it offers a reasonably safe and profitable investment even when conducted within legitimate bounds.

Not a few money-lenders who strenuously opposed the passage of remedial legislation, having tasted the joys of conducting a legal business encouraged by the state and yielding a fair profit, have recently formed themselves into associations which are cooperating with state officials in detecting and convicting violators of these laws and are even employing attorneys to assist the authorities in upholding the constitutionality of the very laws they sought to defeat. This is one of the most gratifying and significant results of the remedial loan movement.

In spite of the great improvement that has taken place within the last few years in the conditions under which the small loan business is conducted, the fact remains that none of these agencies, philanthropic or otherwise, attempts to loan to the workingman at a cost approximating the rate on commercial loans even though some of the profit-making agencies in this field attempt to create such an impression. The lowest cost to the borrower is 12% per annum and in the majority of cases it approximates 24% per annum. Even at this rate many such agencies find it is not easy to return a fair profit on the investment after operating costs have been met. The point should also be emphasized that none of these agencies finds it possible to loan on the sole security of the character of the borrower. They insist that their estimate of his honesty and efficiency be backed up by guarantees in the form of material security or the endorsement of other individuals who appear to be solvent. The question is, can the honesty, trustworthiness, sobriety and industry of an individual serve as a sufficient guarantee for the

repayment of a loan without material security or the endorsement of an employer or creditor and can credit be obtained by such a man on this basis at a rate of charge approximating that prevailing on commercial loans?

There is one type of institution and only one that can advance money to the workingman on security of his honesty and industry and that is the institution which is so close to him as to be able to determine his reliability with fair accuracy—his character becomes the basis of credit only when it can be appraised. Such an appraisal involves an intimate knowledge of his personal habits and of his financial and domestic situation. No capitalistic agency can obtain this knowledge,—it is obtainable only by a man's immediate associates. In other words, character credit for workingmen can come only through mutual protective action by workingmen, that is, through co-operation.

Co-operation comes most easily to men in times of great difficulty. As the Rochdale pioneers united in a plan of distributive co-operation; as the German peasants, workmen and tradesmen united in co-operative credit associations as a means of obtaining credit which as individuals they could not obtain; as the peasants of Ireland united to free themselves from the Gombeen man, so also in this country are workingmen beginning to unite as a means of freeing themselves from the grip of agencies which exploit their necessities, and as a means of obtaining credit on a reasonable basis which now they can obtain, if at all, only at a high price. This form of co-operation which is known in Germany as the Co-operative Credit Association, in Ireland as the Credit Society, in Italy and Canada as the People's Bank, is known in this country as the Credit Union.

The history of modern credit contains no more striking phenomena than the wonderful development of the credit union in Europe in the last 50 years and its tardiness in developing here. The number of credit unions in existence throughout the world at the outbreak of the European war was more than 65,000 with a membership of 15,000,000 people and an annual business amounting to $7,000,000,000. The movement which originated in Germany in 1850 has now spread to practically every European country and even to India, Japan and Egypt. Russia, which in 1904 had 378 of these unions, now has 14,000. The

number in Germany in 1914 was over 18,000, making loans to members in one year of over $1,500,000,000. In 1909, when the first credit union law in the United States was enacted in Massachusetts, there were 40,000 unions operating abroad with an annual turnover of $4,000,000,000. Japan alone had nearly 2,000 unions in 1909 and the little country of Roumania had 2,500 unions with a membership of 350,000 or 35% of the total population of the country, but in that year there was not a single co-operative credit union, rural or urban, in the United States.

Now let us see just what a credit union is. It is an association of persons, united by some common bond or community of interest, joined together in a co-operative endeavor for the following purposes:

1. To encourage thrift by providing a safe, convenient and attractive medium for the investment of the savings of its members.

2. To promote industry, eliminate usury and increase the purchasing power of its members by enabling them to borrow for productive or other beneficial purposes at a reasonable cost.

3. To train its members in business methods and self-government and bring them to a full realization of the value of co-operation.

Under the law of New York—and this is typical of the credit union laws now in effect in eight states in the Union—seven or more persons may combine to organize a credit union in any city, town or rural community. The basis of membership is good moral character—reputation for honesty, sobriety and industry—and identification with the basic unit upon which the credit union is founded, such as employment, neighborhood or fraternal association, membership in the trade union, church club, etc. Dealings are had with members only.

The funds of the credit union consist of the sums paid in by members upon shares or on deposit and of borrowed money. Shares are issued in small denominations—usually $5—and may be paid for in regular weekly or monthly instalments. Each member is required to subscribe for at least one share and is encouraged to subscribe for as many shares as he can afford. Payments upon shares are savings for distant expenditures while deposits are savings for more imminent needs. It is customary to accept even trifling sums on deposit or in payment of shares

in order to encourage saving among the humblest members. Interest is allowed on deposits at, or slightly above, the savings bank rate. Dividends paid upon shares vary. Most credit unions that have attained full headway pay a dividend rate of from 4 to 6% per annum.

In an ordinary joint-stock company the shareholder's money is the main object considered but in a credit union the person of the shareholder is of much greater importance; that is, it is an association of members and not of capital, and for that reason each member has one vote regardless of the number of shares he may hold. The one-man one-vote principle is fundamental to democracy of control. All members share equally in privileges and ratably in profits.

The active management of the credit union is delegated by the general meeting of the members to a board of directors, a credit committee and a supervisory committee, the members of which serve without pay. The directors have the general management of the affairs of the union. They act upon applications for membership, determine the rate of interest upon loans and deposits, and declare dividends. The credit committee has charge of the granting of loans to members and fixes the terms of repayment. The supervisory committee audits the books and accounts and supervises the acts of the directors, officers and credit committee.

A loan that is of no benefit to the borrower is likely to be an unsafe investment. Credit unions, therefore, loan only for productive purposes, and purposes that will effect a saving or supply an urgent need. Loans are commonly made for not more than one year and are repaid in weekly or monthly instalments determined in each instance by the credit committee in conference with the borrower. Ordinarily, loans are secured by the promissory note of the borrower with one or more endorsements of fellow-members, but on small loans endorsements are not usually required. It is the character of the borrower and his endorsers, appraised by the board of directors when the members are admitted to the credit union and again appraised by the credit committee in passing upon applications for loans, that determines the amount of credit extended. The borrower's solvency which

plays such a large part in commercial credit plays but a small part in the determination of credit by a credit union.

In a joint stock bank the shareholders and constituents are mostly different people—a condition which keeps distinct the interests of the buyers and sellers of credit. In a credit union the interests of borrowers and lenders are identical. The very members who pay interest on loans are receiving dividends on their shares. This community of interest enables the credit union to loan with safety upon character alone, for the moral responsibility of repayment is great when a man knows that by violating his obligation he not only withholds the money of a fellow-worker or associate, but invites social ostracism. The mutual responsibility of members and their self-interest causes such supervision over loans as to make the possibility of loss remote. This has been the uniform experience. What few losses have occurred have been due to carelessness and neglect of basic principles. The official reports show that in the 16 years from 1895 to 1910 there were 19 failures out of a total of 15,000 credit unions in Germany and in no single case did a depositor lose a cent. For each one of these failures there were 55 failures among commercial banks.

The credit union avoids any expensive investigation of borrowers. Overhead costs are also reduced by gratuitous service on the part of managing committees and loans can be made at an interest rate which a commercial loaning agency in this field could never approach. The New York credit union law allows a maximum interest charge of 1% per month. In the beginning many credit unions charge the maximum rate but in practice both here and abroad the rate decreases as experience is gained until it approximates that prevailing on commercial loans.

Out of the net profits each year a certain sum usually fixed by the law is set aside to a guaranty fund which provides protection for shareholders, depositors and other creditors in event of loss. The fund is the property of the credit union and no share in it may be claimed by any member except upon the dissolution of the union. It serves as additional loanable capital, making possible a reduction of interest on loans without effecting a reduction in the interest rate paid on deposits or dividends declared upon shares.

The credit union came to the United States by way of Canada, where there are now over 200 credit unions or people's banks in successful operation in the Province of Quebec. The genesis of the Massachusetts credit union law of 1909, the first enacted here, was the successful work of these Canadian associations under the leadership of M. Alphonse Desjardins. There are now some 60 credit unions in operation in Massachusetts. A realization of the need for a central body to extend the system resulted in the organization of the Massachusetts Credit Union formed by a group of philanthropic men and now including in its membership the representatives of a number of the local credit unions. It seeks to secure harmony of action, methods and accounting and by arranging frequent conferences of officials and committees of unions throughout the state offers an opportunity for the interchange of ideas and experiences which is having a most beneficial effect upon the movement in Massachusetts.

Seventeen credit unions are operating in New York City under the law of 1915, in addition to eight unions formed by Jewish farmers.* Among the credit unions in New York City are those formed by the employes of John Wanamaker, the Mutual Life Insurance Co., the Equitable Life Assurance Society, the American Can Co., and the Postal Telegraph Co. Others are operating in groups joined together by neighborhood and fraternal association. Steps are being taken to organize a series of credit unions among the army of employes of the city of New York.† This is testimony to the esteem in which this form of co-operative financial association has already come to be held.

Savings banks, postal savings offices and interest departments of trust companies receive and safeguard the deposits of people who are sufficiently inclined to thrift to journey to these institutions, which are not conveniently located for all, and there stand in line awaiting their turn to deposit. Many a man in order to become thrifty requires a savings agency at his elbow, which not only makes it convenient for him to deposit but introduces the effective element of compulsion contained in the insurance policy and instalment purchase contract. Once a man sub-

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*Twenty-eight credit unions in New York City and nine rural on May 1, 1917.

†New York City Employes Credit Union began business on November 15, 1916.

scribes to an instalment share in a credit union he is not only constantly reminded of his intention to save but is required to live up to his agreement unless he has some excellent reason for not doing so. An indication of the possibilities of the credit union in enticing members to save is contained in the statement, in the last annual report of the Superintendent of Banks of New York, that a single credit union in one year's time had accumulated assets of $36,000. There is no doubt that the savings banks had failed to reach the majority of the men who accumulated this amount of capital.

Consider what it means to a workingman to be able to borrow from a credit union in order to buy for cash certain necessaries of life for which he has been accustomed to pay an unconscionable profit through buying on the instalment plan!

Consider the increased purchasing power of the wages of members joined together in a co-operative purchasing association, buying in large quantities at wholesale such supplies as coal, for example, for retail sale to members, the purchasing association being financed by the credit union! These are matters clearly within the scope of a credit union.

Consider the increased efficiency and improved material condition of the man who has been paying ruinous interest rates to a loan shark for a long time and is able to free himself through the agency of the credit union!

Large numbers of men in the employ of the Postal Telegraph Co. had for years been paying tribute to the loan sharks, who were not only always on hand on pay day to collect their toll—which did not reduce the debt—but followed their victims who sought to escape by going to other cities, by filing claims against their wages, making their lives miserable and often bringing about their dismissal from the service. Many operators were driven to do things they never would have thought of doing had they been free from this curse and they became roving, unstable workmen. Afraid to walk in and out of the front doors of the offices, they dodged through rear entrances, drew their faces into all sorts of shapes so that they could not be recognized,—even changed their names when asking for employment after being dismissed. With the idea of escape from their persecutors many telegraphers requested the trade journal—the *Telephone and Telegraph Age*—

to keep out of its columns any references to their movements from place to place. These requests were filed and came to be known as the "Keep-Out List." According to the testimony of the general manager of the company this condition has been entirely changed through the agency of the credit union. The filing of a claim against a man's wages by a money-lender is now an unusual thing. The "Keep-Out List" no longer exists, and many an operator who struggled for years with the loan shark now walks with head erect in the knowledge that he has a savings account in the credit union and the privilege of borrowing therefrom at a reasonable rate for any legitimate purpose. The benefit which the company has derived from this changed condition is apparent. What it means to the operator and his family in terms of increased earning power, contentment and improved living conditions is no less obvious.

Credit unions are simply associations by means of which men combine to establish local, self-governing institutions of credit to meet their requirements, relying on their own efforts and initiative to work out their own salvation. Success depends upon the character of the members—not upon their financial condition but upon their personal worth. Each member must feel the necessity for the organization, that he is a part of it, that it is his, developed and managed to protect and promote his interests—a real financial democracy of mutual assistance and mutual confidence in which each member is forced to make of his own efforts, his own character and his own habits security worth lending upon. The credit union not only manufactures credit out of the raw material of character but it also manufactures capital synthetically just as nitrate is being reclaimed from the air—making the capital so created available for the legitimate borrowing needs of those who assisted in its accumulation.

It is essentially a social movement which teaches the true uses of credit and inculcates the principles of honesty and punctuality in meeting obligations. It encourages thrift. It increases purchasing power. It eliminates usury and waste. It teaches the real power of co-operation.